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June 22, 2001

Mr. Jeffery C. Berg
Acting Director, Community Development Financial Institutions Fund
U.S. Department of Treasury
601 13th Street, NW, Suite 200 South
Washington, DC 20005

Dear Mr. Berg:

The venture capital partners of one of our clients have requested that we submit their enclosed comments in response to your request for comments published in the Federal Register on May 1, 2001. They are very qualified to comment on the New Markets Tax Credits Program as a result of their experience with similar programs on the state level. They raise venture capital and private-equity funds from the private sector for use in targeted areas (including areas that would be considered low-income communities under IRC Section 45D) and manage such funds under incentive programs using state tax credits similar to the New Markets Tax Credit Program.

They anticipate participating in the New Market Tax Credit Program and intend to request an allocation of tax credits pursuant to IRC Section 45D. Given their experience, if they receive an allocation, they expect to raise the full amount allocated to them shortly after the allocation is made, and would be delighted to meet with representatives of the Community Development Financial Institutions Fund to discuss these comments further and offer any other assistance that you may feel appropriate.

Thank you for your time and consideration. Please contact me for further information on the client, similar programs or if you wish to discuss these comments further.

Sincerely,

John R. Harman III

Enclosure

Comments regarding the New Markets Tax Credit Program --
Section 121(a) of the Community Renewal Tax Relief Act of 2000

Overview and General Comments

Our investment strategy currently envisions establishing a fund under the New Markets Tax Credit Program (the "Program") that would be available for investment in low-income communities, primarily those communities that are within and around the metropolitan areas to which our current funds are dedicated. This would allow us to leverage the deal flow, personnel and infrastructure that we already have in these locations to invest funds raised under the Program efficiently and prudently. It would focus on providing capital of various sources, whether through micro-lending programs, "angel"-level equity investments, or larger lending or equity transactions. This structure should ensure that the benefits of the Program are widely disbursed and that many businesses have an opportunity to receive investments from the fund. Additionally, it will increase the likelihood that the fund can grow to be an independent, self-funding capital source that can continue to provide capital for businesses located in low-income communities long after the sunset of the Program.

1. **IRC §45D(f)(2) requires that in making allocations of NMTCs, priority be given to:**

   (a) any applicant that has a record of having successfully provided capital or technical assistance to disadvantaged businesses or communities or (b) an applicant which intends to satisfy the Substantially All Test by making Qualified Low-Income Community Investments in one or more businesses in which persons unrelated to the CDE hold a majority equity interest.

   (a) How should the Fund implement this policy? For instance, should the fund incorporate preference points into the scoring? Should the Fund make awards to organizations that are deemed competitive and meet one or both of these criteria before providing an allocation to any other applicant?

   We support the idea that preferences should be given to entities that have track records of investing in low-income communities. Under this particular Program, however, the Qualified Community Development Entity ("CDE") is first required to raise the capital to be invested from private sources. As such, the ability to make such investments is entirely predicated on the ability of the CDE to raise such funds from the private sector. Thus, we feel that while a track record of having provided capital and technical assistance to low-income communities is important, a track record of having raised funds from the private sector for such purposes is even more important. It would do little good to make allocations of tax credits to entities that have little chance of actually structuring a capital-raising transaction that would appeal to private sector investors. Those applicants that can demonstrate expertise in structuring such transactions and a history of successfully completing them, especially transactions involving tax credits, should be given great consideration in the allocation process. At a minimum, the Fund should require applicants to provide, as part of the application process, the outline of a capital raising strategy and structure that is well-thought out and likely to succeed.

It is also a good idea to give preference to those entities that intend to provide capital to unrelated parties. This should help ensure the broadest distribution of the benefits of the Program. More qualified, active low-income community businesses are likely to be funded if such a preference is given. We would even support a regulation that prohibited investments by a CDE in businesses that were affiliated with the CDE prior to its investment in the business.

We recommend that allocations be made first to those entities that satisfy both (or in our suggested rubric, all three) preferred categories, with remaining allocations going to those entities that meet at least one of the preferred categories. Only if there is some portion of the total allocation remaining after applicants who fit at least one category have received an allocation would we suggest that applicants who meet neither of the tests receive an allocation.

(b) What specific factors should the Fund consider when evaluating whether an applicant meets the requirements for priority treatment?

As mentioned above, we believe that the historical ability of an applicant to raise capital from the private sector for investment in targeted areas should be the paramount consideration when allocating tax credits under the Program. In addition, the Fund should give preference to those applicants who can demonstrate a successful track record of compliance with other tax credit programs that encourage targeted investment. Analysis of this ability would focus on the amount of funds previously raised by the applicant, the types of areas for which such funds are targeted, the likelihood of its securing investors for the Program and a detailed analysis of how its prior investment activities will coincide or complement its planned activities under the Program. Further, it is our opinion that preference should be given to those applicants that seek to establish a capital source for low-income communities, as compared to applicants that may seek to be capital providers for a particular project or transaction. By creating entities that have funds dedicated to low-income communities, a financial infrastructure can begin to take shape in these communities that can survive the end of the Program and continue to provide capital solutions for the businesses in such areas. Finally, we believe that the Fund should consider the investment experience of the managers of the CDE when making allocations. A critical question is whether the investment professionals involved in the CDE have significant venture capital, loan-making or other investment experience, of the sort necessary to ensure successful execution of the plan presented to the Fund in the CDE's application.

(c) Should more weight be given to one priority category over the other and should an applicant be allowed to receive preference points under both priority categories?

As mentioned above, we believe that an applicant should receive credit under both categories if it qualifies. Both are very important, but we believe that historical ability to raise targeted funds from the private sector is of paramount importance. Given the five year time period during which the CDE has to raise the funds after an allocation, it would be unfortunate to allocate the credits and then have, after five years, a large portion of the credits go unused because the CDE did not have the ability to raise the capital for investment in the low-income communities that it was designed to serve. This would not serve the goals of the Program.

2. Should there be limits as to the amount of a NMTC allocation that may be awarded to an applicant in a calendar year?

The only limitation that we would suggest with respect to allocations is a rule that would prevent a CDE from receiving a new allocation of tax credits until it raises in full the capital associated with any allocations that it had received in previous years. Since the credits are limited by year, there is an incentive to apply for an allocation of credits from each year's statutory allotment. With a CDE having the ability to raise the funds associated with an allocation of tax credits during the five year period after the allocation, there could arise a situation where a CDE has received an allocation and applies for a second allocation before it has completely raised the capital associated with the first allocation. It only seems fair that a CDE not be granted a new allocation until it has demonstrated that it has received Qualified Equity Investments equaling its previous allocations.

3. **During the evaluation process of NMTC applications, the Fund will request that applicants provide information on their track records for providing capital or technical assistance to Low-Income Communities and disadvantaged businesses and the effect that such investment/technical assistance has had on such Low-Income Communities or businesses. Applicants may also be required to describe the social underwriting criteria that they will use when deciding which companies to invest in. If an applicant receives a NMTC allocation, it will be required to report to the Fund on the ways in which the Qualified Equity Investments are used to benefit Low-Income Communities.**

(a) What indicators should the Fund assess when evaluating the community development impact of an applicant's prior activities or the social underwriting criteria of its loan policies?

One of the most important issues for the Fund to evaluate is how consistent an applicant has been in meeting the stated objectives of its earlier targeted funds. If an applicant has raised capital in the past which was to be targeted to a certain geographical area or community, how did the applicant's investments historically match up with its stated objectives? This should give the Fund a good indication of the applicant's ability to comply with the type of requirements that the Program involves.

In addition, the Fund should examine the applicant's plan of operation to establish whether the applicant has a well-conceived plan. Has the applicant identified the particular low-income communities that it wishes to serve? Is its advisory board or board of directors relevant to those areas? Is the applicant's plan of operations something that this particular applicant is likely to achieve? What in its historical operations would lead one to believe that it will be successful in fulfilling its proposed plan?

(b) On what basis should the Fund judge how "successfully" capital or technical assistance has been provided?

Again, we would suggest that the most important indication of an applicant's historical success is its track record of meeting the objectives that it set forth when it first raised capital targeted for certain areas. Its ability to put forth a plan that involves making investments targeted to a certain geographic area or socio-economic group and then executing that plan will be a key indicator in predicting the likelihood of its success under this Program.

(c) What information should the Fund request from allocation recipients as indicators for evaluating the effectiveness of the NMTC Program (*e.g.*, number of jobs created or retained, increases in revenues of businesses receiving Qualified Low-Income community Investments, rates of return to investors from Qualified Equity Investments, or number of clients served at facilities that are developed)?

This information will, of course, depend on the type of investments that are made by the CDE. If, as we intend, the CDE is established as a fund that seeks to invest in low-income communities on a continual basis, it will be very important to track the number of jobs created or retained by the businesses that are funded as well as the financial results of those businesses. Another important statistic that the CDFI should analyze is the amount of capital that is attracted to a business in a low-income community by the investments made by the CDE. Often the greatest economic impact of this type of targeted investment program will come from additional capital that a business is able to attract from traditional sources (*i.e.*, banks, venture capital funds) once it has received initial funding from a non-traditional source such as a CDE. This will help the Fund judge whether the Program is having the results that were originally envisioned. In addition, it will help the Fund guide future allocations to those type of financing structures and initiatives that seem to be having the greatest impact on low-income communities.